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ASX & Media Release

AGL outlines strategic roadmap to deliver improved shareholder returns

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AGL Energy Limited (AGL) has today announced its strategic roadmap to improve return on funds employed (ROFE) and deliver sustainable earnings growth. The strategic roadmap builds on AGL's strengths, and recognises the challenges and opportunities in the existing business and as the energy industry evolves. The strategy will increase business productivity, drive retail profit growth and position AGL for success as the energy industry transforms. It recognises that an organisational transformation will be required, including the creation of an anticipatory culture and a commitment to an orderly transition to a carbon constrained future.

The roadmap builds on AGL's many strengths, including a strong, well-recognised energy brand with over 3.7 million customer accounts; a stable, world-class customer relationship management platform with advanced analytic capability; the largest and lowest cost thermal electricity generation portfolio in the National Electricity Market (NEM); and a large renewable energy portfolio.

Against this backdrop, the retail energy environment is increasingly competitive, consumers are now more aware of their energy consumption, and digital technologies have enabled and increased expectations for price transparency and control.

Additionally, AGL operates in an industry heavily influenced by public policy and regulation. The company will continue to play an active role in promoting competitive neutrality and pro-competitive outcomes in public policies. Important areas of policy reform where AGL is currently focussing include consumer pricing and affordability frameworks; competitive and efficient retail energy markets; and carbon reduction policies. Continuing to address the needs of vulnerable customers remains a priority.

The existing centralised energy supply market is expected to provide near-to-mid term opportunities with an expected increase in wholesale electricity prices, although there are challenges in the long-term from the need to reduce carbon emissions, as well as from increasing penetration of decentralised generation and digital technologies.

AGL recognises that it plays a key role in reducing greenhouse gas emissions, at the same time as providing secure and affordable electricity for Australian households and businesses. AGL released its Greenhouse Gas Policy last month which included a range of commitments and priorities. These commitments will help drive AGL's success by helping mitigate risks to our business, supporting AGL's brand and retail position, and helping attract and retain talent.

In the long-term, energy markets will be transformed by new decentralised products and services, including solar PV, battery storage, connected appliances and smart grids.

AGL understands that it must overcome internal constraints and needs to create an anticipatory culture able to take advantage of opportunities in a changing market environment.

Strategic roadmap

To address the challenges and deliver sustainable earnings growth, AGL's strategy is to harness energy insights to enrich customers. This strategy will be delivered through three key components.

1. Position for Transformation

Operating models of the past need to be changed and new organisational foundations need to be created to position AGL for the transformation occurring in the energy industry.

1.1 Create anticipatory culture

To survive and thrive in the changing environment, AGL will build agile business processes and systems able to anticipate, adapt and position it to take advantage of opportunities as they emerge. This ensures that the company acts entrepreneurially; that it has lean processes; that investments are evaluated rigorously and quickly; that scenario planning is employed; and that the company builds adaptive business partnerships and supply chains. AGL's new organisational structure which was recently announced will facilitate this internal cultural change. The company is also developing a deep and growing talent pool.

2. Drive Productivity

The low growth in centralised energy demand and increasing industry competitiveness is requiring an increased focus on productivity improvements to deliver improved returns.

2.1 Improve capital allocation

AGL is conducting a thorough review of its asset portfolio and targeting around $1 billion in non-strategic and under-performing asset divestments by the end of FY17. Working capital reductions of around $200 million by the end of FY17 are also targeted.

AGL is committed to competing in retail gas markets which requires the company to secure cost-competitive gas supplies. This includes the company's recent Esso/BHP contract, its investment in gas storage and gas exploration and development. The review of the asset portfolio overlaps with the previously announced operational review of the Upstream Gas business. Preliminary recommendations from this review are currently being appraised and expected to be announced shortly.

In the meantime, the company is continuing to assess the Gloucester Gas Project which includes an evaluation of the cost to develop and the expected gas recovery. Proposals from potential suppliers are in the process of being received and reviewed. Once the four Waukivory Pilot wells have been restarted approximately six months' of flow testing will be required before being able to make a final decision.

2.2 Improve operational productivity

AGL will drive an improvement in operational efficiency targeting around $170 million real reduction in its normalised operating cost base, and around $100 million real reduction in sustaining capital expenditure by FY17. AGL is committing to achieve below-CPI cost increases in electricity generation costs over FY16 and FY17.

Total recurring cash benefit targeted by FY17 is around $200 million after netting potential increases to power purchase agreement costs linked to some asset divestments referred to in Section 2.1.

3. Unlock Growth

AGL has significant growth opportunities both in its core retail business and in new closely-related businesses as new energy technologies become increasingly economic.

3.1 Grow retail energy's share of value

The retail energy market in the NEM is highly competitive, but remains relatively unsophisticated compared with other retail industries, such as telecommunications and banking. AGL has been successfully executing its retail growth strategy since June 2014 and will continue differentiating its retail business through initiatives which include:

- Applying sophisticated customer segmentation to focus customer acquisition, retention, loyalty and product and service innovation to drive higher customer value;
- Digital solutions to better meet customers' needs in a low-cost way; and
- Differentiating with new capabilities, such as AGL's digital meter capability and battery storage business, ahead of major retail competitors.

3.2 Invest in business models which exploit new technology

AGL's New Energy business has been established to embrace the major changes transforming the energy industry and to create new business models to meet customers' needs.

AGL intends to create one million 'smart' connections to consumers and businesses by 2020 by scaling to become one of the leading providers of metering services, rooftop solar, commercial energy services, energy storage and electric vehicle services.

AGL is well-placed to succeed in this new and changing environment given its large customer base, intimate knowledge of its customers' needs, its strong brand, sound balance sheet, and highly motivated and committed employees.

FY15 Outlook

AGL has reconfirmed the FY15 Underlying Net Profit after Tax (Underlying Profit[1,2]) guidance range of $575-$635 million and subject to normal trading conditions, the result is expected to be in the top half of the range.

Contributing to the solid performance have been generation volumes above expectations, some wholesale price improvement, and a better than expected performance from the Macquarie Generation acquisition.

As a consequence of the organisational review currently in progress total restructuring costs of approximately $30 million (pre-tax) are expected to be booked as a significant item in FY15.

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[1] Underlying Profit is the statutory net profit after tax adjusted for significant items and changes in the fair value of certain financial derivatives.

[2] Moranbah is classified as "held for sale" and, in accordance with accounting standards, is no longer depreciated. If at 30 June 2015 Moranbah is not sold and is no longer classified as held for sale, then non-cash depreciation of approximately $25 million (pre-tax), for the period 1 January 2014 to 30 June 2015, would need to be recognised. No profit on sale is assumed for providing Underlying Profit guidance.

Further inquiries:

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About AGL

AGL is one of Australia's leading integrated energy companies and is the largest ASX listed owner, operator and developer of renewable energy generation in the country. Drawing on over 175 years of experience, AGL operates retail and merchant energy businesses, power generation assets and an upstream gas portfolio. AGL has one of Australia's largest retail energy and dual fuel customer bases. AGL has a diverse power generation portfolio including base, peaking and intermediate generation plants, spread across traditional thermal generation as well as renewable sources including hydro, wind, landfill gas and biomass. AGL is taking action toward creating a sustainable energy future for investors, communities and customers.